IN THE HIGH COURT OF PUNJAB AND HARYANA AT CHANDIGARH

Income Tax Appeal No.73 of 2005
Date of decision: September 12 , 2006

Commissioner of Income-tax (Central), Ludhiana

v.

M/s Avery Cycle Inds. Ltd., Ludhiana

Present: Mr.S.K.Garg, Advocate for the respondents.
Mr.Akshay Bhan, Advocate for the respondent.

CORAM:
Hon'ble Mr.Justice Adarsh Kumar Goel
Hon'ble Mr. Justice Rajesh Bindal

Rajesh Bindal, J.

This appeal by the revenue is directed against order dated 21.9.2004, passed by the Income-tax Appellate Tribunal, Chandigarh Bench `B' (for short, `the Tribunal') in I.T.A. No. 967/Chandi/96, for the assessment year 1993-94, raising the following substantial questions of law:

> "(i) Whether on the facts and in the circumstances of the case, the Tribunal was right in law in holding expenses of Rs.1,55,795/- spent on silver vessels, carpets, silver ornaments and other gift items for distribution to the dealers as business expenditure?
>
> (ii)Whether on the facts and in the circumstances of the case, the Tribunal was right in law in deleting the disallowance of interest of Rs.2,43,000/- on the ground that there is no direct nexus between the borrowings and interest free advances made to certain parties?
>
> (iii) Whether on the facts and in the circumstances of the case, the Tribunal was right in law in directing to consider interest income as forming part of business profits for computing deduction u/s 80HHC?
>
> (iv) Whether on the facts and in the circumstances of the case, the Tribunal was right in law in directing to exclude ST/CST, discount receipts, amounts written off and claim receipts from the total turnover for computing deduction u/s 80 HHC of the I.T.Act?"

Question No. (i)

Regarding question No.(i), the Assessing Officer, while framing the assessment, disallowed the claim of the assessee of a sum of Rs. 1,55,795/- on account of expenses claimed under the head “Sale Promotion Expenses” on account of silver vessels, carpets, silver ornaments and other gift items distributed to the dealers, who visited the factory of the assessee from time to time. The claim of the assessee was that distribution of such gifts is customary in nature. The claim was rejected on two counts-- first, no evidence was produced to the effect that gift items were actually distributed amongst dealers and secondly, reliance was placed on a judgment of Kerala High Court in Commissioner of Income-Tax v. Alleppey Co. Ltd., (1994) 207 I.T.R. 598, wherein it was held that expenditure incurred on account of presentation of curios to foreigner buyers visiting the factory amounts to entertainment expenses.

In appeal, the assessee failed before the Commissioner of Income-tax (Appeals) [for short, `the CIT (A)'].

The Tribunal, while referring to the judgments of this Court in H.M.M. Limited v. Commissioner of Income-Tax, (1998) 231 ITR 726 and Avon Cycles Private Limited v. Commissioner of Income-Tax, (1999) 238 ITR 85, relied upon an order passed by it in the case of the assessee for the assessment year 1992-93 and held that expenditure incurred on distribution of gift articles to various dealers was for business consideration as it does promote goodwill among the dealers for the assessee.

After hearing the counsel for the parties and also going through the orders passed by the authorities, we are of the view that distribution of gift articles to dealers would certainly fall within the ambit of expenditure for business consideration. The dealers selling the product of a manufacturer are certainly its life line and if some reasonable amount is spent on distribution of some gifts to them that certainly promotes goodwill and enhances business interests, hence, the

same cannot, in any way, be termed as entertainment expenditure. In I.T.A.No.328 of 2004-- Commissioner of Income Tax-I, Ludhiana v. M/s Varinder Agro Chemicals Ltd., Ludhiana, decided on 17.8.2006, while dealing with an issue regarding distribution of gifts on festivals, this Court held that the same was not a kind of entertainment expenditure. Keeping in view the nature, quantum of business and the profits generated out of it, a sum of Rs. 1,55,795/- spent by the assessee on presentation of gift items to dealers cannot be held to be a non-allowable expenditure. Accordingly, we reject the plea of the Revenue and answer the question against it and in favour of the assessee.

Question No. (ii)

As far as question No.(ii) is concerned, the Assessing Officer, during the course of assessment, found that during the year in question, the assessee advanced a sum of Rs.13,50,000/- to its Managing Director without any business purpose. The advance was not carrying any interest. On scrutiny of the profit and loss account, it was found that large number of loans of different types were outstanding against the company on which it incurred liability of Rs. 2,52,50,890/- on account of interest. Accordingly, the Assessing Officer disallowed the amount of interest on interest free advance to the Managing Director for non-business purposes. In addition to this, it was found that certain other amounts were also advanced to various other Directors without any interest for non-business purposes. Interest thereon was also disallowed.

In appeal before the CIT(A), the assessee failed. The Tribunal accepted the appeal of the assessee by relying upon its earlier order of the assessment year 1992-93.

We have already dealt with an identical issue in the case of Commissioner of Income Tax, Ludhiana v. Abhishek Industries Ltd., Ludhiana, I.T.A. No.110 of 2005, decided on 4.8.2006, wherein it is held that where the assessee is found to have advanced certain sums to sister concerns for non-

business purposes and on the other hand is incurring interest liability on various loans raised by it, interest on the loans raised to that extent cannot be held to be for business purposes. Following the reasons recorded therein, we answer the question in favour of the Revenue and against the assessee. Appeal of the Revenue is accepted while upholding the disallowance made by the Assessing Officer on that account.

Question No. (iii)

Regarding question No. (iii), while framing the assessment, the Assessing Officer found that the assessee had received interest of Rs. 4,98,344/- from the Income-tax Department; Rs. 4,90,000/- from the Punjab State Electricity Board on security deposits and Rs. 6,935/- on security amount deposited for car. The claim of the assessee that this forms part of the business receipts as the same was integral part of the business activity of the company was considered and rejected by the Assessing Officer for the purpose of calculation of deduction under Section 80HHC of the Income-tax Act, 1961 (for short, `the Act').

The CIT(A), referring to the judgments of Rajasthan and Delhi High Courts in Commissioner of Income-Tax v. Rajasthan Land Development Corporation, (1995) 211 I.T.R. 597 and Commissioner of Income-Tax v. Cement Distributors Ltd., (1994) 208 I.T.R. 355 respectively, rejected the appeal of the assessee on this issue.

The Tribunal, referring to an order passed by Mumbai Bench of the Tribunal, accepted the plea of the assessee on this ground.

The term “profits of the business” has been defined in Explanation (baa) to Section 80HHC of the Act, which reads as under:

> “(baa) “profits of the business” means the profits of the business as computed under the head “Profits and gains of business or profession” as reduced by -
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> (1)ninety per cent of any sum referred to in clause (iiia), (iiib) and (iiic) of section 28 or of any receipts by way of brokerage, commission, interest, rent, charges or any other receipt of a

similar nature included in such profits; and

(2) the profits of any branch, office, warehouse or any other establishment of the assessee situate outside India."

As far as question of addition of the amount of interest of the kind received by the assessee for the purpose of computation of business is concerned, in our view, the answer thereto is clearly available in the definition of "profits of the business", contained in clause (baa) of Section 80HHC of the Act, as reproduced above, from where it is evident that "profits of the business" means the profits and gains of business or profession, as computed under the head "profits and gains of business or profession" as reduced by the items, provided for in the definition. A perusal of the assessment order shows that while dealing with the deductions under Section 80-HHC of the Act, receipt of interest by the assessee from Income-tax Department; on securities from Punjab State Electricity Board and on security deposit for car was held to be not connected with the business activity and the Assessing Officer treated the same as income from other sources. However, while computing the income from business or profession, the amount of interest so earned by the assessee, as mentioned above, was taken as part of the business income only and the same was not reduced therefrom for dealing under the head "income from other sources". While considering the appeal filed by the assessee on this issue, the CIT(A) rejected the same. Before the Tribunal, the assessee succeeded.

Once at the time of passing of the assessment order in computing the income from business or profession, the amount of receipt of interest, as mentioned above, has been shown and assessed as income from business or profession, there is no reason for reducing the same out of the income from business or profession for the purpose of calculation of deduction under Section 80HHC of the Act, as after including the same in the income from business or profession, the reduction, as envisaged under that provision, would be carried out. This is clear even from what the Tribunal has directed. Accordingly, we do not find any merit in this

contention of the Revenue and hold that once the income is assessed as income from business or profession, the same has to be taken as such for the purpose of calculation of profits of the business in terms of clause (baa) of Section 80HHC of the Act after reducing therefrom 90% of the amount, so referred in the clause.

Question No. (iv)

Regarding question No.(iv), the Assessing Officer found that during the year in question, the assessee had received claim of Rs. 2,57,011/-; written off balance of Rs. 40,098/-; receipt discount of Rs. 33,677/- and other miscellaneous receipts were Rs. 7,24,931/-. Besides this, the assessee had collected central sales tax/ sales tax to the tune of Rs. 20,82,041/-. The claim of the assessee that these items be not treated as part of the total turnover was rejected by the Assessing Officer and it was ordered that the same be treated as part of the total turnover for the purpose of calculation of benefit under Section 80HHC of the Act.

As is evident from the order of the CIT(A), the inclusion of Rs. 7,24,931/- on account of miscellaneous receipts was not contested by the assessee. The CIT (A), while confirming the disallowance on account of claims and discounts received, reversed the disallowance on account of balance written off. As far as receipt of sales tax/central sales tax is concerned, on that account also, the order of the Assessing Officer was upheld.

The Tribunal, without there being much discussion, reversed the order passed by the authorities below merely by referring to an earlier order passed by it. As far as consideration of sales tax and excise duty, being part of the total turnover for the purpose of calculations under Section 80HHC of the Act is concerned, this Court in I.T.A. No.293 of 2005—Commissioner of Income-Tax-I, Ludhiana v. M/s Vardhman Polytex Ltd., Ludhiana, decided on 22.5.2006, has already decided the issue in favour of the revenue and against the assessee. Following the same, we uphold the order passed by the Tribunal and reject the ground of appeal on that account.

As far as question of claims received and discount receipts is concerned, the claim of the assessee is that a sum of Rs. 2,57,011/- was received from the Insurance Company on account of claim for damage to the car and Rs.33,677/- were on account of discount received in respect of purchase of chemical from M/s Canning Mitra Phoenix. In our view, the amount of insurance claim and discount receipt received by the assessee during the year in question on account of damage to the car does not form part of the turnover of the assessee for the purpose of calculation of deduction under Section 80HHC of the Act. Car is not the commodity in which the assessee is dealing in and the discounts received in respect of purchases made will reduce the cost of purchases and will not add in the receipt side.

Accordingly, the question is answered in favour of the assessee and against the Revenue.

The appeal is disposed of in the manner indicated above.

(Rajesh Bindal)
Judge

(Adarsh Kumar Goel)
Judge

September 12 , 2006
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